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IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

CHARLES L. GRIMES,

Petitioner,

v.

VITALINK COMMUNICATIONS CORPORATION,

Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of Delaware

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

When property is taken under state authority, the "just compensation" to the owner mandated by the Fifth and Fourteenth Amendments includes both (a) "taking compensation," *i.e.*, the value of the property of which the owner was deprived at the time of taking, and (b) "post-taking compensation," the value of the use of the property of which the owner was deprived from the time of taking to the entry of judgment. *E.g.*, *Seaboard Air Line Ry. Co. v. United States*, 261 U.S. 299 (1923).

1. Is compensation "just" that calculates post-taking compensation by using an arbitrary "interest rate" wholly unrelated to the actual earning power of which the owner was deprived during the post-taking period?

2. Specifically, where the taken property is corporate stock, is compensation "just", which is ascertained by employing one number for the earning power of the stock in calculating the first element of compensation, to the *detriment* of the stockholder, and refusing to employ the same number for the earning power in calculating the second element when doing so would *help* the stockholder?

PARTIES TO THE PROCEEDING

The names of all parties appear in the caption of the case. Petitioner is an individual.

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PETITION FOR A WRIT OF CERTIORARI

Charles L. Grimes respectfully petitions the Court for a writ of certiorari to review the judgment of the Supreme Court of Delaware in this proceeding.

I. CITATIONS BELOW, JURISDICTION, AND STATUTES INVOLVED

This case in the lower courts is reported at *Grimes* v. *Vitalink Communications Corp.*, C.A. No. 123334, 1997 WL 538676 (Del. Ch. Aug. 26, 1997), and *Grimes* v. *Vitalink Communications Corp.*, 708 A.2d 630 (Del. 1998). The opinion of the Supreme Court of Delaware was issued on April 1, 1998. This Court has jurisdiction under 28 U.S.C. § 1257.

The case involves the due process clause of the Fourteenth Amendment to the Constitution of the United States and the just compensation clause of the Fifth Amendment to the Constitution of the United States, together with the appraisal provisions of the Delaware Corporation

Law, 8 *Del. Code* § 262; all of which are printed in the Appendix ("App.").

II. STATEMENT OF THE CASE

Petitioner Grimes held 200,000 shares in respondent Vitalink Communications Corporation. More than 90% of Vitalink's stock was acquired by a subsidiary of another company pursuant to a tender offer (which Grimes did not accept). Delaware law allows a 90% stockholder to "squeeze out" the remaining stockholders by forcing a merger upon them, but permits dissenting stockholders to obtain the fair value of their stock through an appraisal action brought against the corporation in the Delaware Court of Chancery. 8 *Del. Code* §§ 251, 262 (App. 42a – App. 62a). Exercising the authority of a 90% owner, the acquiring company forced a merger of itself into Vitalink, effective July 1, 1991, thus converting Vitalink into a wholly-owned subsidiary of its parent. Grimes dissented from the merger and his strenuous objections to settlement of a fraud, non-opt out class action were disregarded. He accordingly brought an appraisal action.

The Court of Chancery awarded Grimes a sum for the value of his stock at the time of taking that was arrived at, so far as here material, by calculating the present value of Vitalink's forecasted cash flow over the next five years, employing as the discount rate for the present value calculation a figure reflecting the earning power that had been accepted by the boards of both Vitalink and the acquiring company, and used by both of their investment bankers. This figure was relatively high (20.83%); since the higher the discount rate the lower the present value, use of such a figure

worked to the advantage of the company by reducing the compensation payable to Grimes.[1]

However, in calculating compensation to Grimes for the post-taking period the Court of Chancery refused to use this figure for the earning power of which Grimes was deprived during that period, employing instead a much lower arbitrary rate based on the legal rate of interest. App. 22a - App. 38a. It gave no reason for assuming that the earning power of which Grimes was deprived should have fallen off by some two-thirds immediately after the taking, nor for applying the 20.83% rate when doing so benefitted the company yet refusing to apply it when doing so would benefit the stockholder. (It also refused to consider evidence of Grimes's own individual track record with comparable investments, which was a much higher number. App. 27a - App. 29a).

Grimes appealed to the Supreme Court of Delaware. It affirmed in a two sentence order. App. 1a - App. 2a. Hence this petition.

III. REASONS FOR ALLOWANCE OF THE WRIT

The questions presented are important ones that warrant consideration by this Court. They deal with the ascertainment of "just compensation" for a taking of property pursuant to state law, under the Fourteenth Amendment, which imposes upon the states the same requirements as the Fifth Amendment

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[1] The present value of a stream of future payments for a given time period is that sum which, invested at a given interest rate, would produce the same amount at the end of the time period as the cumulative value of that stream of payments, earning interest at that given rate. The higher the assumed interest rate (called the "discount rate"), the lower the present value. (In lay terms, the greater your earning power, the less you need at the outset to reach the same goal.) Thus, the present value of $1000 a year for five years at 10% is $3790.79, while at 20% it is only $2990.61.

imposes on the United States. *Olson* v. *United States*, 292 U.S. 246, 254 (1934). In particular, they deal with the ascertainment of just compensation in a specific type of taking: the "squeezeout" of dissenting stockholders in a corporate merger. This is a particularly timely and important question as the economy moves into a new wave of "mega-mergers."

A. This Court Should Make It Clear That in Ascertaining "Just Compensation" for the Taking of Property, a Court Cannot Refuse to Consider the Earning Power Which the Property Would Have Had in the Owner's Hands After the Taking and Before Payment of Compensation.

Since *Seaboard Air Line Ry. Co.* v. *United States*, 261 U.S. 299 (1923), it has been established that "just compensation" for taken property has two components. The first component is compensation for the property itself, *i.e.*, its ascertained value at the time of taking (for convenience we refer to this herein as the "taking value"). The other component is the value which the owner was deprived of between the time of taking and the payment of compensation. "The Government's obligation is to put the owners in as good position pecuniarily as if the use of their property had not been taken," *Phelps* v. *United States*, 274 U.S. 341, 344 (1927); only inclusion of such a component can "ensure that [the owner] is placed in as good a position pecuniarily as he would have occupied if the payment had coincided with the [taking]." *Kirby Forest Indus., Inc.* v. *United States*, 467 U.S. 1, 10 (1984).

This second component–for convenience we will call it herein the "post-taking deprivation value"–is commonly referred to as "interest" and measured by applying a

percentage rate to the taking value. But it is *not true interest*, *i.e.*, payment for the use of money. Rather, it is compensation for what the owner would have earned on the taken property during the post-taking period.[2]

The first component, the *taking value*, is normally measured by reference to a hypothetical construct, "fair market value," *i.e.*, the cash bargain a hypothetical willing seller of the taken property would strike with a hypothetical willing buyer. *E.g.*, *United States* v. *Miller*, 317 U.S. 369, 373-75 (1943). The second component, the *post-taking deprivation value*, by contrast, is specific to the property and the owner. In order to put the owner into "as good position pecuniarily as he would have been if his property had not been taken," *Seaboard*, 261 U.S. at 304, it reflects the actual money's worth[3] it would have meant to the owner–not some postulated hypothetical owner, but the particular real individual in question–to have had the property in hand during the post-taking period. It reflects the earning power that the owner was deprived of during the limited period from the time of taking to the time of payment. The underlying principle is identical to that set forth in *Kimball Laundry Co.* v. *United States*, 338 U.S. 1 (1949), that compensation for such a deprivation for a limited period is to be determined with reference to the deprivation suffered by the specific

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[2] Accordingly, when the United States takes property it must pay post-taking compensation as part of "just compensation" notwithstanding the general rule (now codified to 28 U.S.C. § 2516(a)) that interest on a claim against the United States is not allowed absent agreement or special statute. *Seaboard*, *supra*. "It is not a claim for interest within the purpose or intention of [28 U.S.C. § 2516(a)]." *Phelps* v. *United States*, 274 U.S. at 344.

[3] Not, of course, mere sentimental or idiosyncratic "value to the owner," but tangible or "transferable" value.

owner. There, this Court held that just compensation for a temporary taking of business premises, thereby shutting down the business, must take into account not only the rental value of the property but the going-concern value of the business.

Beyond the implications of *Kimball Laundry* when taken together with the principle of *Seaboard*, this Court has never given guidance as to the ascertainment of post-taking deprivation value, and in particular as to the role to be played by the specifics of the taken property and the owner's own experience. Some courts have played fast and loose as a result. Thus, disregarding the basis for compensation expressed by this Court, the Court of Claims and its successors have generally employed a uniform fixed "interest" rate for specific periods for all owners without regard for individual circumstances, expressing "a strong judicial policy in favor of uniform rates to apply to all those entitled to" post-taking compensation. *E.g.*, *Hughes Aircraft Co.* v. *United States*, 31 Fed. Cl. 481, 492 (1994), *aff'd*, 86 F.3d 1566 (Fed. Cir. 1996), and cases cited. The theory of this approach is that to do otherwise would discriminate against some owner; but in fact the approach obviously discriminates against owners who would have made a substantial return on their investments and confers a windfall on those who would

not. And it is manifestly contrary to the basic principles articulated by this Court.[4]

Guidance from this Court on this subject is thus clearly needed.

B. In Particular, This Court Should Make It Clear That in Ascertaining "Just Compensation" for the Taking of Stock in a Forced Merger "Squeezeout," a Court Cannot Refuse to Consider the Earnings Rate at Which the Stock Itself Was Valued

A specific element of this general subject of valuing post-taking deprivation on which the Court's guidance is needed and timely is its application to "squeezeouts" of minority stockholders, as in the case at bar.

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[4] In many taking cases–reflecting no doubt the fact that the majority of such cases deal with fairly routine real property condemnations–the owners appear not to have offered evidence of specific earning power and to have been content with the legal interest rate as the measure of post-taking compensation. *E.g.*, *Seaboard*, *supra*; *Phelps*, *supra*. But it is clear that such an arbitrary statutory rate is not to be forced on an unwilling owner, and that, constitutionally, at the owner's instance post-taking compensation must be tailored to fit the deprivation suffered by the particular owner in the particular case. Thus, in the Declaration of Taking Act of 1931, 46 Stat. 1421, 40 U.S.C. § 258a, Congress decreed a flat 6% rate for post-taking "interest." The courts rejected this effort, interpreting the statute as setting a floor but not a ceiling, *e.g.*, *United States* v. *Blankinship*, 543 F.2d 1272 (9th Cir. 1976); *United States* v. *329.73 Acres of Land*, 704 F.2d 800 (5th Cir. 1983); and rejected a 1986 effort by Congress to replace the 6% rate with one based on 52-week Treasury bills. *United States* v. *50.50 Acres of Land*, 931 F.2d 1349 (9th Cir. 1991). (We do not necessarily endorse the method of ascertaining compensation, which the courts there applied in lieu of the statutory rates, however.)

The rights of stockholders *inter se* are for many purposes deemed to arise from a contract among them adopting the provisions of the corporate documents and the general corporation law of the state of incorporation. But the widely disseminated investment-backed expectations of stockholders are not deemed to be subject to arbitrary forfeiture no matter what the particular provisions of a general corporation law may be, so that a "squeezeout" of a minority stockholder is a compensable "taking" of his shares, which is subject to the requirements of due process. *Beerly* v. *Department of the Treasury*, 768 F.2d 942, 948 (7th Cir.), *cert. denied*, 475 U.S. 1010 (1985); *cf. Offield* v. *New York, New Haven & Hartford R.R. Co.*, 203 U.S. 372 (1906). The "squeezeout" provisions of state corporation laws[5] are thus subject to the overriding constitutional principles of just compensation; and in particular to the requirement of compensation for post-taking deprivation.

Delaware makes provision of post-taking "interest" wholly discretionary with the court in an appraisal action. *Alabama By-Products Corp.* v. *Cede & Co.*, 657 A.2d 254, 267 (Del. 1995). That is not enough; as we have seen, due process *mandates* the award of such "interest." And, to repeat, the rate of such "interest" must be sufficient to "put [the squeezed-out stockholder] in as good position pecuniarily as he would have been if his property had not been taken." *Seaboard*, 261 U.S. at 304. In light of the principles of *Seaboard* and *Kimball Laundry*, that position must be ascertained on the basis of the actual earning power of the property in the stockholder's hands on the facts of the particular case. It is manifestly irrational not merely to reject evidence of what the squeezed-out stockholder himself earned

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[5] And federal ones, too. *Beerly* involved a national bank and the "squeezeout" provisions of the National Bank Act.

on similar investments, but to refuse to apply the very earning power that the stock was found to have in the very same case.[6]

There are other factors in the evaluating of stock taken in a "squeezeout" that merit this Court's consideration. One in particular is the posture of the parties. While the distinction between taking for a "public use," which is permissible, and a "private use," which is not, has been drastically attenuated in recent years, *e.g.*, *Hawaii Housing Auth.* v. *Midkiff*, 467 U.S. 229, 239-44 (1984), surely a corporate "squeezeout" such as the present one is about as close to the edge as possible. (Here there is not even the public interest in a public utility that justified the taking in *Offield*, *supra*.) This implies a balancing of interests different from that applicable when the sovereign takes property for the public. In a compulsory purchase by the sovereign, "[j]ust compensation means a compensation that would be just in regard to the public, as well as in regard to the individual," *Bauman* v. *Ross*, 167 U.S. 548, 570 (1897); "'just' both to [the] owner whose property is taken and to the public that must pay the bill." *United States* v. *Commodities Trading Corp.*, 339 U.S. 121, 123 (1950). Such solicitude for the interests of the taker is inappropriate where, as here, the taker is not the sovereign

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[6] To carry forward the example in footnote 1, suppose the forecasted cash flow per share for the next five years was $1000 a year, and the earning power of the stock was reckoned at 20% a year. A share would then be valued at $2990.61. Suppose further that two years elapsed between the time of taking and the payment of compensation. During that period, the stockholder has been deprived of at least what the earning power of the stock (20% per year compounded) would have produced when applied to $2990.61, or $1315.87. If for this compensation he were nevertheless arbitrarily limited to a rate of, say, 6%, he would receive only $369.64 in compensation for his lost $1315.87. That is essentially what the courts below did here.

for the benefit of all, with the cost of taking falling on the public fisc, but a corporate majority exercising its muscle to cram a merger down the throats of a dissenting minority. In particular, the private, one-on-one posture of a "squeezeout" underscores the impropriety of determining post-taking deprivation value on the basis of some generalized formula applicable to all owners of all kinds of property.

And while a taking authorized by law is not a tort, in such circumstances it is appropriate to look to such concepts from tort law as that the defendant takes the plaintiff as he finds him, and to estop the majority from denying to the "squeezed-out" stockholder the benefit of the same earning rate as it applied in valuing the stock.

Finally, we repeat the salient feature of this particular case. The Constitution mandates *just* compensation. How can compensation be "just," which applies one level of earning power to the first element of compensation, to the *detriment* of the stockholder, and refuses to apply the same level of earning power to the second element when that would *help* the stockholder?

CONCLUSION

The questions involved are important, warrant this Court's attention, and are very timely in view of the rising wave of corporate mergers. The petition for certiorari should be granted.

Respectfully submitted,

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